

## Internal Revenue Service

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Date:  
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TY:

Taxpayer =  
Employer =  
State X =  
C percent =

Dear :

This letter responds to your request for a private letter ruling dated March 23, 2011, in which you request the following rulings: (1) the premiums paid by Taxpayer for private supplemental unemployment insurance under the plan described below are trade or business expenses deductible under § 162 of the Internal Revenue Code; and (2) the benefit payments under the private supplemental unemployment insurance purchased under the plan described below are not included in Taxpayer's gross income under § 61.

### FACTS

Taxpayer is an employee of Employer in State X. Employer provides certain employees with an opportunity to voluntarily purchase supplemental unemployment insurance on an after-tax basis. Taxpayer will participate in the supplemental unemployment insurance program. The cost of the insurance coverage is at prevailing market rates and is based on the experience rating attributable to the individual's employment. Employer may exclude certain employees based on certain criteria, such as the employee's employment history.

A participant in Employer's supplemental unemployment insurance program may elect to purchase the insurance through voluntary withholding from his or her paycheck. The participant directs Employer to remit the premium payments to the insurance carrier on his or her behalf. The premiums are paid on an after-tax basis, after Employer

withholds employment taxes. Participants purchase the supplemental unemployment insurance without involvement from Employer. The insurance coverage is portable if the participant changes employment to another employer, although the cost of the insurance coverage may change based on the experience rating at the participant's new employment.

The State X Department of Insurance has approved the insurance coverage for policies issued by at least one insurance company, and approval is pending for another insurance company. The insurance may also be purchased by other licensed insurance companies under similar arrangements.

The benefits under the proposed insurance contract will supplement the State X Unemployment Insurance Law ("UIL") benefits. The insurance contract will pay benefits to ensure that the participant receives C percent of his or her pre-unemployment wages should the participant become unemployed. Eligibility under Employer's program is tied to benefit eligibility under the State X UIL; benefits will not be paid unless the participant is currently eligible to receive State X unemployment benefits and is not currently fully employed.

Under the State X UIL, unemployment benefits are paid only to a claimant who is totally unemployed and who is unable to engage in his or her usual employment or in any other for which he is reasonably capable. The State X UIL further provides that no benefits shall be payable to any claimant who is not capable of work or who is not able to work in his or her usual employment. Accordingly, individuals who are eligible for state disability benefits, because of an inability to work, are not eligible for state unemployment benefits. Furthermore, voluntary separation from employment generally does not entitle a person to unemployment benefits under the State X UIL.

Therefore, a participant is not eligible for benefits under the insurance contract when the loss of the covered employment is due to illness or disability. Furthermore, the insurance contract only covers involuntary unemployment from full-time employment. While State X UIL benefits are available in limited cases of voluntary separation from employment (such as caring for a sick spouse), the insurance contract further limits benefits and does not cover any voluntary separation from employment or other separation from employment due to non-occupational hazards.

Benefits payable under the insurance contract will be paid periodically and begin after a participant has received state unemployment benefits for two weeks. Benefits will cease at the earlier of the cessation of State X state benefits or 24 weeks of payments under the insurance contract. The policy never pays benefits for a longer period than that provided by the State X UIL, but a participant may contract for a shorter period of benefits. The premiums are not placed in a fund or trust established and contributed by potential beneficiaries. There is no cash surrender value of the policy.

## LAW AND ANALYSIS

Ruling Request (1)

Section 162(a) of the Internal Revenue Code allows a taxpayer to deduct all ordinary and necessary business expenses paid or incurred during the tax year in carrying on any trade or business.

Section 262 provides that a taxpayer generally may not deduct personal, living, or family expenses.

It has long been recognized that an employee is engaged in the business of being an employee, and that expense which is essential to the continuance of the employment is deductible for income tax purposes. *Noland v. Commissioner*, 269 F.2d 108 (4<sup>th</sup> Cir. 1959); *Schmidlapp v. Commissioner*, 96 F.2d 680 (2<sup>nd</sup> Cir. 1938). Furthermore, an employee is engaged in the trade or business of performing services as an employee separate and apart from the performance of those services for his existing employer. *Motto v. Commissioner*, 54 T.C. 558 (1970); *Primuth v. Commissioner*, 54 T.C. 374 (1970); Rev. Rul. 75-120, 1975-1 C.B. 55. Because an employee's trade or business exists apart from the employee's performance of services for one particular employer, expenses that an employee incurs in seeking new employment in the same trade or business are deductible, as are expenses an employee incurs in suing a former employer for wrongful termination. Rev. Rul. 75-120, *supra*; *Biehl v. Commissioner*, 118 T.C. 467 (2002), *affd.* 351 F.3d 982 (9<sup>th</sup> Cir. 2003).

Rev. Rul. 81-193, 1981-2 C.B. 52, considered whether contributions by employees to private plans for payment of non-occupation disability benefits under the New Jersey Temporary Disability Benefits Law are deductible business expenses. In reaching the conclusion that the expenses are not deductible business expenses, but are rather nondeductible personal expenses, that ruling concluded that:

Amounts paid by employees to fund private plans for the payment of disability benefits are not paid or accrued in carrying on a trade or business because they are incurred to provide indemnity coverage for loss of wages due to unemployment from nonoccupational hazards rather than from business hazards. The nonoccupational personal nature of the benefit aspect of the private disability plans makes the contributions to the private plans nondeductible personal expenses under section 262. [Emphasis added.]

In this case, the premiums paid under the insurance contract are intended to insure wage continuation at a level based on Taxpayer's existing salary for a stated benefit period during which the taxpayer is unemployed. The premiums are analogous to the types of contributions to insure against business contingencies that Rev. Rul. 81-193

strongly inferences are deductible. The insurance contract provides indemnity coverage for lost wages due to unemployment resulting from occupational or business hazards. It is a recognized aspect of employment that an employee may be terminated for business reasons. The insurance contract insures against this occupational risk and permits the taxpayer to carry on in the trade or business of being an employee.

Since the insurance contract provides indemnity coverage for lost wages due to unemployment resulting from occupational or business hazards, the premiums paid by Taxpayer for the insurance contract described above are business expenses deductible under § 162(a).

#### Ruling Request (2)

Section 61(a) provides that, except as otherwise provided by law, gross income includes all income from whatever source derived. Accordingly, a taxpayer must include in gross income an accession to wealth, unless it is excluded from income by another section of the Code.

Any benefits Taxpayer receives under the supplemental unemployment insurance contract are an accession to wealth. Further, there are no exclusions from gross income of benefits received under a supplemental unemployment insurance policy in the Code. Thus, the entire amount of any benefits received under the insurance policy are includible in Taxpayer's gross income under § 61.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

These rulings are directed only to the taxpayer requesting them. Section 6110(k)(3) provides that they may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

R. Matthew Kelley  
Assistant to the Branch Chief, Branch 2  
(Income Tax & Accounting)

cc: